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UNITED STATES OF AMERICA 97 FERC

FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, Linda Breathitt,
and Nora Mead Brownell.

Islander East Pipeline Company, L.L.C. Docket Nos. CP01-384-000
CP01-385-000
CP01-386-000

Algonquin Gas Transmission Company Docket No. CP01-387-000

PRELIMINARY DETERMINATION ON NON-ENVIRONMENTAL ISSUES

(Issued December 21, 2001)

1. On June 15, 2001, Islander East Pipeline Company, L.L.C. (Islander East) filed an application in Docket No. CP01-384-000 under section 7(c) of the Natural Gas Act (NGA) and Part 157 of the Commission's regulations for a certificate of public convenience and necessity to: (1) construct, own, and operate a new interstate pipeline to transport gas in Connecticut and New York; and (2) lease capacity from Algonquin Gas Transmission Company (Algonquin). In addition, in Docket Nos. CP01-385-000 and CP01-386-000, Islander East seeks a blanket construction certificate under Part 157, Subpart F, of the Commission's regulations, and a blanket transportation certificate under Part 284, Subpart G, of the Commission's regulations, respectively. In Docket No. CP01-387-000, Algonquin filed an application under NGA section 7(c) and Part 157 of the Commission's regulations, for a certificate of public convenience and necessity to construct facilities in Connecticut and lease the capacity that is created to Islander East. We find issuing this preliminary determination is in the public interest because it provides certainty concerning the economic aspects of Islander East's and Algonquin's proposals.

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3. We are making a preliminary determination on the non-environmental issues in this proceeding. These findings support issuance of certificates to Islander East and to Algonquin, subject to the conditions discussed below. However, this order does not consider or evaluate any of the environmental issues in this proceeding. Those issues are still pending and will be addressed in a subsequent order when the environmental review and analysis are complete. Thus, final approval and issuance of the certificates is

dependent on a favorable environmental review and nothing in this order limits our actions regarding our environmental analysis.
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5. I. Proposal
6.
7. Islander East proposes to construct and operate a pipeline that will extend from an interconnection with Algonquin's existing C-System near North Haven, Connecticut, across Long Island Sound and terminate near Brookhaven, New York on Long Island.[1] Islander East intends to provide transportation service to the KeySpan Gas East Corporation, d/b/a KeySpan Energy Delivery Long Island (KeySpan Long Island) and The Brooklyn Union Gas Company, d/b/a KeySpan Energy Delivery New York (KeySpan New York). In addition, Islander East intends to provide transportation service to two power producers: (1) AES Endeavor, a division of AES Corporation (AES Calverton) and (2) Brookhaven Energy Limited Partnership, an affiliate of American National Power (ANP Brookhaven).

1. Algonquin's existing pipeline system extends from points near Lambertville and Hanover, New Jersey through New Jersey, New York, Connecticut, Rhode Island, and Massachusetts to points near Boston, Massachusetts. Algonquin proposes to construct facilities to create capacity on its existing C-System that will be leased to Islander East.[2]
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3. A. Islander East
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5. Islander East proposes to construct: (1) approximately 44.8 miles of 24-inch pipeline from North Haven, Connecticut to Brookhaven, New York; (2) approximately 5.6 miles of 24-inch pipeline from the proposed Islander East mainline near Wading River, New York to the AES Calverton plant (the Calverton Lateral); (3) a meter station near Brookhaven for deliveries to the KeySpan Long Island distribution system and to the ANP Brookhaven plant; (4) a meter station at the end of the Calverton Lateral for deliveries to the AES Calverton plant; and (5) other appurtenant facilities. Islander East states that the estimated cost of the proposed facilities is $149.6 million.
6. Islander East states that the facilities it proposes to construct are designed to transport 260,000 Dth per day on a firm basis and up to 285,000 Dth per day when

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[1]Islander East is a limited liability company formed under the laws of Delaware, with its principle place of business in Houston, Texas. Islander East's members, with equal ownership rights, are Duke Energy Islander East Pipeline Company, L.L.C. and KeySpan Islander East Company, L.L.C.

[2]Algonquin and Islander East are affiliates. Algonquin is a subsidiary of Duke Energy Corporation (Duke Energy). One of Islander East's members is Duke Energy. Islander East Pipeline Company, L.L.C., is also a subsidiary of Duke Energy.

factors change on Algonquin's system. Islander East conducted an open season between January 29 and February 28, 2001, and executed precedent agreements, all for ten-year terms, totaling 260,000 Dth per day with KeySpan Long Island, KeySpan New York, ANP Brookhaven, and AES Calverton. The precedent agreements with KeySpan Long Island and KeySpan New York allow them to phase-in their volumes, with a maximum and minimum level of service, over the first five years of their contracts.[3] The precedent agreements with ANP Brookhaven and AES Calverton are fixed throughout the terms of service.[4] By 2008, Islander East anticipates transporting a total of 445,000 Dth per day for its four initial shippers. The following table summarizes the transportation commitments that Islander East has with its four initial shippers for the first five years of service:

7.

Customer	Maximum Daily Transportation Quantity (in Dth per day)					
	11/1/03	11/1/04	11/1/05	11/1/06	11/1/07	11/1/08
ANP Brookhaven	90,000	90,000	90,000	90,000	90,000	90,000
AES Calverton	60,000	60,000	60,000	60,000	60,000	60,000
KeySpan Long Island (maximum)	60,500	82,500	112,750	134,750	162,250	162,250
KeySpan Long Island (minimum)	60,500	71,500	92,000	114,000	138,000	162,250
KeySpan New York (maximum)	49,500	67,500	92,250	110,250	132,750	132,750
KeySpan New York (minimum)	49,500	58,500	75,500	93,000	112,000	132,750
Maximum MDTQ	260,000	300,000	355,000	395,000	445,000	445,000
Minimum MDTQ	260,000	280,000	317,500	357,000	400,000	445,000

1. Islander East states that it recognizes that the proposed facilities will need to be expanded to meet its shippers' requirements and, when necessary, will file additional

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[3]The precedent agreements with KeySpan Long Island and KeySpan New York require that changes to maximum daily transportation quantities be specified by the shipper at least six months prior to the effective date.

[4]AES Calverton has the right to reduce its maximum daily transportation quantity (MDTQ) of 60,000 Dth per day by up to 20,000 Dth per day on or prior to December 31, 2002. ANP Brookhaven has the right to reduce its MTDQ of 90,000 Dth per day by up to 40,000 Dth per day on or prior to June 1, 2002.

applications to install compression and/or pipeline looping when final capacity commitments are made.

2.

3. In addition to the proposed construction, Islander East proposes to lease 285,000 Dth per day of capacity on Algonquin's C-System from an interconnection with Algonquin's mainline near Cheshire, Connecticut to the proposed interconnection with Islander East's system near North Haven.[5] Islander East will use the capacity to provide firm and interruptible transportation for its shippers under the term of Islander East's FERC Gas Tariff. The lease provides for an initial term of twenty years and year-to-year thereafter unless terminated by Islander East by written notice no less than two years prior to the end of the initial term or two years prior to the expiration of any subsequent one year term. Islander East will pay Algonquin a fixed monthly lease charge of $334,135 and a monthly operating and maintenance charge of $32,307.[6] In addition, Islander East will pay its share of all property-related taxes levied on Algonquin's C-System estimated to be $387,840 per year. The lease charge is designed to recover the cost of the incremental facilities to be constructed by Algonquin. All lease-related charges are contained in Islander East's cost of service and are reflected in its recourse rates.

4.

5. Islander East proposes to provide firm transportation service under Rate Schedule FTS and interruptible transportation service under Rate Schedule ITS pursuant to rates, terms and conditions set forth in its pro forma FERC Gas Tariff. Islander East proposes to offer negotiated rates and recourse rates. Islander East states that its recourse rates are cost-based using the straight fixed-variable rate design. Islander East's pro forma tariff states that any negotiated rate can be less than, equal to, or greater than the maximum recourse rate, but not less than the minimum recourse rate. Islander East states that the terms and conditions contained in its pro forma FERC Gas Tariff conform to the requirements of the Commission's Order Nos. 636 and 637.

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[5]In a November 13, 2001 response to a data request, Algonquin clarified that under the lease agreement Islander East would lease 260,000 Dth per day on a firm basis and 25,000 Dth per day on an interruptible basis. The interruptible service will be subordinate to the rights of the firm shippers on Algonquin's C-System.

[6]The monthly operating and maintenance charge will be adjusted annually, based on the Gross National Product Implicit Price Deflator.

7. B. Algonquin

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9. Algonquin proposes to: (1) construct a new compressor station at the beginning of its C-System near Cheshire, Connecticut, consisting of a 10,310 horsepower Solar Taurus 70 gas turbine and associated facilities, (i.e., aboveground piping, tool launchers, buildings, fencing, and pavement) (Cheshire Compressor Station); (2) retest and upgrade its C-System pipelines from the current maximum allowable operating pressures (MAOP) of 750 psig to a MAOP of 814 psig; (3) repair two segments of pipe, each 25 feet in length, on the C-1 pipeline in New Haven County, Connecticut; and (4) remove two pig launchers from an existing facility in New Haven County, Connecticut and relocate them at the new Cheshire Compressor Station. Algonquin states that the estimated cost of the project is approximately $32.3 million.

1. The proposed facilities and upgrading of existing facilities will provide 260,000 Dth per day of additional capacity on Algonquin's C-System. Algonquin proposes to lease this capacity to Islander East under the terms discussed above. Algonquin states that the revenues it will receive from Islander East under the lease will compensate it for the costs associated with the proposed facilities.

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3. II. Procedural Issues

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5. A. Notice and Interventions

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7. Notice of Islander East's applications was published in the Federal Register on June 28, 2001 (66 Fed. Reg. 34,436 - 34,437). In Docket Nos. CP01-384-000, CP01-385-000, and CP01-386-000, thirty-one parties filed timely, unopposed motions to intervene. Twenty-two parties filed motions to intervene out-of-time.[7] Notice of Algonquin's application was published in the Federal Register on June 28, 2001 (66 Fed.

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[7]They are: Town of Branford, Connecticut; Town of Brookhaven, New York; Christine Chiocchio; Vincent J. Chiocchio; Rebecca and Stanley Mars; William G. Lazine; Kevin J. McGuire; Edward Avery, Marietta Cherpak, and Deborah Lagatolla; Raymond J. Gincavage; United States Postal Service; David Schaffer; Save the Sound, Inc.; Edward P. Lang; New York State Department of Environmental Conservation; Connecticut Office of Consumer Counsel; Connecticut Department of Public Utility Control; Pine Orchard Association; Town of North Haven, Connecticut; Henry M. Lewis; Tilcon Inc. and Branford Steam Railroad; Town of Guilford, Connecticut; and the Connecticut Siting Council.

Reg. 34,435 - 34,436). Twenty parties filed timely, unopposed motions to intervene. Eight parties filed motions to intervene out-of-time.[8]
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9. Timely unopposed motions to intervene are granted by operation of Rule 214 of the Commission's Regulations.[9] Additionally, the Commission finds that granting the motions to intervene out-of-time will not delay, disrupt, or otherwise prejudice this proceeding or place an additional burden on existing parties. Therefore, for good cause shown, these late-filed motions to intervene in this proceeding are granted. The Appendix to this order lists all interveners.
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11. B. Comments, Protests, and Subsequent Actions
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13. Comments in support of Islander East's proposals in Docket Nos. CP01-384-000, CP01-385-000, and CP01-386-000 were filed in the interventions of Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc. (jointly, Consolidated Edison); KeySpan Delivery Companies;[10] Northeast Utilities Service Company, on behalf of Yankee Gas Services Company (Yankee); and PanCanadian Energy Services Inc. (PanCanadian). In general, the supporting comments state that there is a need for additional pipeline capacity in New York City and on Long Island. Further, the commenters asserted that the project will enhance the availability of both eastern and western Canadian gas supplies and provide reliability and flexibility to New England customers through a more integrated pipeline grid. Also, they assert that the new facilities will, according to commenters, allow access to growing markets in Connecticut.
14. The Public Service Commission of the State of New York (New York PSC) commented that if proposals announced by Tennessee Gas Pipeline Corporation and Iroquois Gas Transmission System, L.P. to cross Long Island Sound are filed on a timely basis, the Commission should evaluate them in conjunction with the Islander East project. Southern Connecticut Gas Company and Connecticut Natural Gas Corporation (jointly Connecticut Companies) filed a joint intervention opposing the Islander East applications. On November, 20, 2001, the Connecticut Attorney General filed an

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[8] They are: William G. Lazine; Raymond J. Gincavage; Edward Avery, Marietta Cherpak, and Deborah Lagatolla; Connecticut Office of Consumer Counsel; Connecticut Department of Public Utility Control; the Town of North Haven, Connecticut; Town of Guilford, Connecticut; and the Connecticut Siting Council.

[9] 18 CFR § 385.214 (2001)

[10] The KeySpan Delivery Companies consist of KeySpan Long Island and KeySpan New York as well as Boston Gas Company, Colonial Gas Company, EnergyNorth Natural Gas, Inc., and Essex Gas Company (collectively, KeySpan Energy NE).

untimely protest to Islander East's and Algonquin's requests for a preliminary determination.
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16. The KeySpan Delivery Companies, Yankee, and PanCanadian filed comments in support of Algonquin's proposal that reiterate the supporting arguments filed in the Islander East applications. Comments opposing Algonquin's application were filed by Calpine Energy Service, L.P. (Calpine) and New England Local Distribution Companies (New England LDCs). Protests to Algonquin's proposal were filed by Consolidated Edison, Northeast Energy Associates (Northeast Energy), and the Connecticut Companies.
17.
18. Islander East and Algonquin filed individual motions for leave to answer and answers to the timely filed protests and comments filed to their respective applications. On December 4, 2001, Islander East and Algonquin individually filed a motion for leave to answer and answer the untimely protest filed by the Connecticut Attorney General. Although the Commission's procedural rules prohibit answers to protest, we may, for good cause, waive this provision.[11] We find good cause to do so in this instance in order to insure a complete record in this proceeding. The parties' protests, comments, and responses are addressed below.
19.
20. Numerous landowners, landowner and environmental groups, municipal governments, and state agencies have filed interventions or comments stating their concerns or opposition to the Islander East and Algonquin filings. These comments concern various environmental issues, including: the impact on property values and existing business operations, the impact on wildlife and vegetation, the impact on wetlands and Long Island Sound, the impact to shellfishing, safety, the impact on water wells and septic systems. Many of these parties request that the Commission examine alternate locations and routes. This preliminary determination will discuss all non-environmental issues concerning the project. An environmental impact statement (EIS) is being prepared and will address all the environmental concerns raised by the parties. It will also address alternative locations and routes for the Islander East project. A subsequent Commission order will discuss the findings of the EIS.
21.

[11] 18 CFR § 385.213(a)(2)(2001).

22. C. Requests for Hearing and Technical Conference

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24. The Connecticut Companies ask that the Commission either convene an evidentiary hearing, deny Islander East's project, or condition the project to satisfy their concerns. An evidentiary, trial-type hearing is necessary only where material issues of fact are in dispute that cannot be resolved on the basis of the written record.[12] Here, there are no material issues of fact in dispute that would necessitate an evidentiary hearing. The record, including the applications, responses to data requests, and the pleadings, contains sufficient information and data to make a reasoned decision on the merits preliminarily approving the proposals. Thus, no purpose would be served by conducting an evidentiary hearing and the request for a hearing are denied.

1. Northeast Energy requests that the Commission hold a technical conference to discuss the rate and service issues raised in its intervention. Again, the record contains sufficient information to make a reasoned decision. The request is denied.

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3. D. Preliminary Determination

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5. As stated, on November 20, the Connecticut Attorney General filed a protest to Islander East's request in its June 15 application for the Commission to issue a preliminary determination by December 31, 2001. Generally, he contends that it is inappropriate for the Commission to issue a preliminary determination because Islander East can not minimize the adverse effects of the project on Algonquin's existing customers or the affected landowners and communities. Other individuals filed similar requests advocating that the Commission not issue a preliminary determination until it has completed its environmental review of the project.

6.

7. The Commission's general policy is to issue preliminary determinations in major construction cases. Under this phased approach, the Commission issues an order making a preliminary determination as to whether issuance of a certificate authorizing project construction would be in the public convenience and necessity, based solely on non-environmental issues. The Commission has stated that "this phased approach to consideration of the application promotes administrative efficiency and ensures timely consideration of certificate applications in furtherance of the Commission's regulatory obligations and competitive policy goals and objectives."[13]

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[12] See, e.g., Southern Union Gas Co. v. FERC, 840 F.2d 964, 970 (D.C. Cir. 1988); Cerro Wire & Cable Co. v. FERC, 677 F.2d 124 (D.C. Cir. 1982); Citizens For Allegan County, Inc. v. FPC, 414 F.2d 1125, 1128 (D.C. Cir. 1969).

[13] See TransColorado Gas Transmission Co., 53 FERC ¶ 61,421 at 62,494 (1990).

9. Basically, a preliminary determination facilitates the planning process on a pipeline project so that the needs of the market are met in a timely fashion. However, the preliminary determination does not compromise the Commission's environmental review under the National Environmental Policy Act (NEPA). As stated, as part of the environmental review of the Islander East project, the Commission will issue a draft EIS addressing the environmental concerns raised by interveners and commenters. The draft EIS will be sent to all interveners, commenters, local governmental agency, and other interested parties. All individuals will have an opportunity to file comments on the draft EIS. The Commission will consider those comments and incorporate them into a final EIS.

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11. When the final EIS is complete, the Commission will review its findings and issue a final order in this proceeding. No environmental disturbance may occur based upon the issuance of a preliminary determination. The findings in a preliminary determination are contingent upon the completion of the environmental review and the issuance of a final order. We find that there is no reason to delay the issuance of a preliminary determination in this proceeding. To the extent the protest and commenters raise non-environmental issues, we find that the record is sufficient to address these issues at this time and they are addressed below.

12.

13. III. Discussion

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15. Since the applications pertain to facilities used for the transportation of natural gas in interstate commerce subject to the jurisdiction of the Commission, Islander East's and Algonquin's proposals are subject to the requirement of subsections (c) and (e) of section 7 of the NGA.

16.

17. A. Project Need and the Certificate Policy Statement

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19. On September 15, 1999, the Commission issued a Policy Statement to provide guidance as to how we will evaluate proposals for certificating new construction.[14] The Policy Statement established criteria for determining whether there is a need for a proposed project and whether the proposed project will serve the public interest. The Policy Statement explains that in deciding whether to authorize the construction of major new pipeline facilities, the Commission balances the public benefits against the potential adverse consequences. Our goal is to give appropriate consideration to the enhancement of competitive transportation alternatives, the possibility of overbuilding, subsidization by existing customers, the applicant's responsibility for unsubscribed capacity, the avoidance of unnecessary disruptions of the environment, and the unneeded exercise of eminent domain in evaluating new pipeline construction.

1. Under this policy, the threshold requirement for pipelines proposing new projects is that the pipeline must be prepared to financially support the project without relying on subsidization from the existing customers. The next step is to determine whether the applicant has made efforts to eliminate or minimize any adverse effects the project might have on the applicant's existing customers.

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3. The Commission also considers potential impacts of the proposed project on other pipelines in the market and those existing pipelines' captive customers, or landowners and communities affected by the route of the new pipeline. If residual adverse effects on these interest groups are identified after efforts have been made to minimize them, the Commission will evaluate the project by balancing the evidence of public benefits to be achieved against the residual adverse effects. This is essentially an economic test. Only when the benefits outweigh the adverse effects on economic interests will the Commission then proceed to complete the environmental analysis where other interests are considered.

4.

5. 1. Subsidization

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7. The Commission's Policy Statement directs that the threshold requirement for pipelines proposing new projects is that the pipeline must be prepared to financially support the project without relying on subsidization from existing customers. Islander East is a new pipeline company that has no existing customers. As such, the threshold requirement is not applicable to Islander East's proposal.

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[14]Certification of New Interstate Natural Gas Pipeline Facilities (Policy Statement), 88 FERC ¶ 61,227 (1999); order clarifying statement of policy, 90 FERC ¶ 61,128 (2000); order further clarifying statement of policy, 92 FERC ¶ 61,094 (2000).

8.

9. Several parties raise various issues concerning Algonquin's lease that they contend may ultimately result in a subsidization by existing customers. These issues include: (1) an appropriate depreciation rate for the leased facilities; (2) the allocation of operating and maintenance (O&M) costs and property taxes; (3) the adequacy of the proposed pre-tax return; and (4) the proper assessment of fuel costs related to the use of the new compressor facilities.

10.

11. As discussed below, the Commission finds that to protect Algonquin's existing customers from subsidizing the lease arrangement with its affiliate Islander East, Algonquin must depreciate its facilities based on a five percent rate, corresponding to the 20-year lease life. Further, Algonquin will be required to treat the lease arrangement as an incremental rate, recording the costs and revenue separately, including a separate fuel tracker, and will not be able to roll the costs into its system rates. Further, to insure that other similarly situated shippers can receive a similar financial lease arrangement as Islander East, Algonquin will be required to offer the same financial lease arrangement to all similarly situated shippers. Therefore, as conditioned, we find that Algonquin existing customers will not subsidize its proposed expansion.

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13. 2. Benefits and Impact

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15. a. Benefits

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17. Islander East maintains that it developed its project to meet the needs of the New York City and Long Island market area. According to Islander East, the executed precedent agreements for almost all of the initial capacity of the project demonstrate a need for the project in those areas. Islander East also asserts that its facility is ideally located to facilitate the development of needed generation projects on Long Island.[15] Further, Islander East contends that the proposed pipeline will increase the reliability of natural gas supply in the area by adding a separate pipeline that will deliver gas to Long Island from the east side of the New York City and Long Island service area. As such, it contends that its proposed pipeline will avoid the existing bottlenecks on the distribution systems that deliver gas from the west side of the service area.

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[15]The New York Independent System Operator (NYISO) issued a report in March 2001, that concluded that, by 2005, New York City needs 2,800 MW of new generating capacity and Long Island needs 1,800 MW. NYISO reliability rules require nearly all new generation needed to meet New York City and Long Island requirements be located on Long Island. Islander East states that if all of its capacity were used to fuel gas-fired combined cycle electric generators, it would be sufficient to supply 1,500 MW of generation.

18.

19. Islander East also claims that its project will diversify the gas portfolio delivered to Long Island. Traditionally, it states that Long Island has received its gas from western Canada and the U.S. Gulf Coast. Islander East asserts that its proposed pipeline will access supplies from the Gulf Coast, Mid-Continent, Chicago, and Canada through Algonquin's interconnections. Also, via Algonquin and Maritimes & Northeast Pipeline, L.L.C., Islander East will be able access recently developed offshore gas supplies from Nova Scotia. Islander East contends that this new gas supply will add to the reliability of the Long Island pipeline delivery network. Further, Islander East avers that an increase in the number of pipelines and supply sources serving a market will enhance the price competition of gas in that market.

20.

21. The Algonquin lease eliminates the need for Islander East to construct approximately 27 miles of duplicative and environmentally disruptive pipeline facilities to connect with Algonquin's mainline. In addition, Algonquin states that the project will increase the value of secondary firm transportation on its system by adding an additional market area. Algonquin further asserts that the project will increase the reliability and flexibility of its existing services and enhance its flexibility during the summer maintenance period.

22.

23. Mr. Jerry C. Shaw questions whether Islander East's customers truly need their contracted volumes. He states that two non-existent power plants have precedent agreements with Islander East. He argues that those facilities may never be built. Mr. Robert W. Kohlus also questions the need for an electric generation facility that would be served by the Calverton Lateral. When a natural gas pipeline has a contract with one or more shippers, the Commission does not look behind those contracts to assess the certainty that an end-use shipper will actually require the service.[16] However, it does require that the pipeline execute contracts for the level of service and for the terms of service represented in the precedent agreements prior to commencing construction.[17] The Commission is reasonably assured that if a company executes a contract and commits to paying for service, it has a need for the gas service under contract.

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[16] See, e.g., Transcontinental Gas Pipe Line Corp., 82 FERC ¶ 61,084 at 61,316 (1998).

[17] See, e.g., Transcontinental Gas Pipe Line Corp., 92 FERC ¶ 61,285 at 61,975 (2000).

25. b. Cost to Existing Customers and Pipelines
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27. Islander East states that this project will not have an adverse impact on other pipelines and their captive customers because it will serve incremental load. Islander East points out that for the period 1995 to 2000, throughput on KeySpan Long Island has grown at a rate of eight percent per year and throughput on KeySpan New York has grown at 3.13 percent per year. This represents a combined annual average growth rate of 4.7 percent over that period of time. Islander East states that growth in the KeySpan New York and KeySpan Long Island service areas is expected to increase at a 3.1 percent annual average rate between 2000 and 2010.

1. Algonquin indicates that the project will not result in operational or economic impact to its existing customers. It states that existing customers will enjoy increased reliability and flexibility of service due to the addition of compression and the resulting increase in pressure on the C-system. Algonquin also asserts that the project will have no adverse effect on existing pipelines and their captive customers because no other pipeline currently serves Islander East. In fact, Algonquin asserts that pipelines currently interconnected with Algonquin will benefit from the additional marketing opportunities presented by Islander East.
2.
3. The Connecticut Companies state that there will be no benefits for Connecticut residents. They argue that there are no proposed delivery points in Connecticut and that the project is taking supply from Connecticut and flowing it to New York. The Connecticut Companies also state that the proposed pipeline has no provisions for bi-directional flow to serve Connecticut and the northeast markets. In response, Islander East states that through backhaul and displacement transactions it is well positioned to provide fully-integrated access between New York and New England. It asserts that Islander East can serve Connecticut when such service is requested
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5. Similarly, the Connecticut Attorney General contends that the project will not increase mainline natural gas capacity into the region, but instead will use existing gas supplies transported on a pipeline paid for by Connecticut consumers for the benefit of Long Island consumers, limiting the ability to meet electricity demands and raising the price of natural gas in Connecticut.
6.
7. It is the responsibility of the Islander East shippers to obtain upstream capacity. They cannot displace existing firm shippers on Algonquin's system. Algonquin stated that shippers that wish to move gas to Islander East can acquire capacity on its system through capacity release, contract with Algonquin for firm backhauls, or by purchasing

gas from those parties holding capacity rights on Algonquin.[18] Similarly, Islander East states that on Algonquin's system, its shippers may use their existing contracted capacity (if any) with secondary delivery points, new firm capacity, released capacity, interruptible capacity, or purchase gas on a bundled basis where Algonquin's mainline connects with its C-System.[19]

8.

9. The Connecticut Attorney General's claim that Islander East shippers will use existing gas supplies and bid up prices to Connecticut consumers is confusing. Islander East has noted that the Algonquin system and its existing interconnections allow shippers to take advantage of gas supplies from many parts of the US and Canada, including new gas supplies from offshore Nova Scotia. We also note that the expansion of Algonquin's C-System will be paid for by Islander East, not by Algonquin's existing customers in Connecticut. Nevertheless, those Connecticut customers will benefit from the expansion by being able use the capacity created on Algonquin's C-System when it is not in use by Islander East at no additional capital cost.

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11. c. Cost to Landowners

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13. Islander East states that the proposed route for its pipeline involves approximately 50 miles of pipeline, approximately 28 miles on land and 22 miles in Long Island Sound. Islander East asserts that approximately 87 percent of the land route will use or run parallel to existing utility corridors. Islander East states that it has met with public officials, communities, and landowners, and, as a result, has made modifications to its project design to address the concerns of these groups. Algonquin's proposal will primarily affect the area around the site of its new Cheshire Compressor Station.

1. Islander East has not obtained any easements yet, but expects to obtain easements on 256 parcels of land totaling 314.8 acres. Algonquin states that it has obtained 50 acres for its new compressor station and must still obtain easements on five parcels of land totaling 0.81 acres. Islander East and Algonquin state that they are continuing the "consultative process" with potentially affected parties which could result in the adoption of route alternatives or deviations. Therefore, according to both applicants, the easement negotiation process is still in the planning phase. Islander East and Algonquin contend that they intend to engage in good faith discussions and work with affected landowners to reach agreement without the use of eminent domain. Both applicants note that some limited use of eminent domain rights may be necessary, but typically only for property

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[18] See Algonquin's September 28, 2001 response to question 3 of September 7, 2001 data request.

[19] See Islander East's September 24, 2001 response to question 2 of September 7, 2001 data request.

that is (1) in probate, (2) held by multiple landowners, (3) held by non-responsive, out-of-state landowners, (4) owned by unidentified landowners, or (5) encumbered with defective title records.
2.
3. Mr. Raymond J. Gincavage filed comments in response to Islander East's assertion that it anticipates acquiring all of its easements without eminent domain. He contends that this is a gross distortion of the truth. He asserts that he does not intend to negotiate an easement for his property and that many other landowners also have no intention of granting easements.
4.
5. d. Project Need and Certificate Policy Statement Conclusion
6.
7. As stated, the Islander East project can proceed without subsidies. Further, as discussed, above we find that the proposed project will not adversely affect or degrade service to Algonquin's existing shippers. Further, the Commission finds that the Islander East project will provide benefits that outweigh any adverse impacts arising from the lack of negotiated easements. Notably, the Islander East project will fill an immediate market need as evidenced by the long term precedent agreements for over 90 percent of its design capacity. Further, the Islander East project is well situated to serve, via low cost expansion, expected growth in the Long Island and New York City market areas. Also, Algonquin's existing customers will be able to access the Long Island and New York City markets on a secondary basis via Islander East.
8.
9. Moreover, the Islander East project will increase the reliability and flexibility of the interstate pipeline grid by offering more direct access to existing and new gas supply sources and increased availability to gas and electric generation markets in the Long Island and New York City markets. This should also result in more price-competition, and potentially lowering natural gas prices in these markets as well. Finally, as noted, the Algonquin lease eliminates that necessity for Islander East to construct approximately 27 miles of new pipeline facilities, thereby avoiding disruption to the environment.
10.
11. Therefore, consistent with the Policy Statement and NGA section 7, we preliminarily find approval of Islander East's and Algonquin's proposals to be in the public convenience and necessity. As stated, we will require Islander East to execute contracts for the level of service and for the terms of service represented in the precedent agreements prior to commencing construction.
12.
13. B. Part 284 Service vs. Leased Capacity
14.
15. Generally, several parties question whether Algonquin's lease arrangement with Islander East is appropriate as opposed to a transportation service agreement. Calpine asserts that Algonquin does not explain why the service to Islander East could not be

offered under Algonquin's Part 284 rate schedule for lateral service, Rate Schedule AFT-CL, instead of leasing capacity. Calpine asserts that the lease creates different classes of customers using the same facilities which may constitute unduly discriminatory treatment. Calpine adds that lease arrangements should not become a means to circumvent the prohibition on the negotiation of terms and conditions of pipeline service in Order No. 637. Calpine asks that if the lease is approved, Algonquin must be required to offer the same terms and conditions to similarly situated shippers.

16.

17. The Connecticut Companies argue that the lease allows Islander East, Algonquin's affiliate, to reap the benefits of facilities that Algonquin's existing customers have paid for over a number of years and to pay for only a small fraction of their actual value. It contends that although the lease payments cover Algonquin's actual costs, they do not come close to recovering the system average cost or the actual value of the service. It avers that Algonquin's customers will lose out on the opportunity for significantly higher revenue contributions. Additionally, the Connecticut Companies argue that Algonquin's lease will increase the cost to serve future markets in Connecticut because low cost expandability on Algonquin's facilities has been essentially given away under the Algonquin lease.

18.

19. Consolidated Edison contends that Algonquin's existing customers would subsidize the Islander East lease because under Algonquin's proposal the lease payment that would cover the cost of the incremental capacity, but not any of the costs of the existing facilities. Consolidated Edison believes that the lease would allow Algonquin to retain all profits from the lease as opposed to existing customers realizing the benefits through lower rates established in Algonquin's next NGA section 4 rate case. Consolidated Edison asserts that the lease is essentially an incremental rate proposal and that Commission policy does not permit incremental rates lower than system average rates

20.

21. Algonquin maintains that the commenters are using an inappropriate benchmark when comparing the lease payments to Algonquin's generally applicable Part 284 rate schedule. Algonquin states that, in contrast to its Part 284 shippers, Islander East does not have access to secondary receipt and delivery points, cannot offer its leased capacity as released capacity, and cannot share in Algonquin's interruptible revenues. Algonquin believes that the commenters are also basing their opposition to the lease payment structure under the mistaken premise that if Islander East were a Part 284 shipper rather than a lessee, they would benefit from a rolling-in of costs at a later date. Algonquin asserts that the Commission's Certificate Policy Statement advocates incremental rates, not rolled-in treatment, for lateral lines and lateral line expansions.

22.

23. The Commission finds that Algonquin's proposed service is strictly incremental construction and transportation service. Islander East through the lease agreement is

paying for the cost to construct the incremental facilities to provide service. The proposal will not provide Islander East with access to Algonquin's system, just the C- System for which it is making lease payments. If Islander East seeks capacity on other segments of Algonquin's system, it will be required to pay the appropriate rate.
24.
25. In Texas Eastern Transmission Corporation,[20] the Commission determined that it would consider applications to acquire upstream or downstream capacity on other pipelines on a case-by-case basis. The Commission explained that it foresaw a number of potential benefits arising from such acquisitions. One of those benefits is to reduce duplicative and unnecessary facilities, which is consistent with the Commission's goal of meeting new demand with both less cost and less environmental impact.

26. For rate purposes, the Commission generally approves lease agreements for a pipeline to hold capacity on another pipeline where the lease payments paid by the lessee are found to be less than, or equal to the lessor's firm transportation rates of comparable service over the term of the lease on a net present value basis.[21] The Commission determines what the alternative rate is, and whether the lease results in a lower rate than not approving the lease and also whether the lease provides a benefit to the leasee's rate payers. We find that the Islander East lease will result in a lower rate that if Islander East had constructed the required facilities. Accordingly, we will approve the lease agreement. However, to insure that other similarly situated shippers are eligible for the same financial arrangements based on depreciation expense, property taxes, and operation and maintenance expenses that Algonquin has offered its affiliate in the Lease Agreement, Algonquin is required to offer the same type of Lease Agreement and financial terms to any similarly situated shipper.[22]
27.
28. C. Rate Issues
29.
30. 1. Islander East's rate proposal

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[20]74 FERC ¶ 61,074 at 61,220-21 (1996).

[21]See Midwestern Gas Transmission Co. (Midwestern), 73 FERC ¶ 61,320, at 61,888 (1995); Mobile Bay Pipeline Projects, 55 FERC ¶ 61,358, at 62,078 (1991). See also Colorado Interstate Gas Co., 76 FERC ¶ 61,291 (1996), Columbia Gas Transmission Corp., 78 FERC ¶ 61,030 (1997).

[22]We also note that when the lease agreement expires and the capacity converts back to Algonquin, Islander East will need to request abandonment authorization for the leased capacity and Algonquin will need certificate authorization to use the capacity as part of its existing capacity.

1. To provide the proposed transportation service, Islander East will offer firm transportation service under its proposed Rate Schedule FTS and interruptible transportation service under Rate Schedule ITS. Shippers subscribing to firm transportation service will be given the option of paying a negotiated rate or a cost-based recourse rate under the FTS Rate Schedule. Islander East proposes an initial recourse rate for firm transportation of $9.868 per Dth, which is based on the straight fixed-variable rate design methodology. The initial rate for interruptible transportation service will be a 100 percent load factor commodity rate of $0.3244 per Dth. Islander East reports that since it expects to have only 260,000 Dth per day of its total of 285,000 Dth per day capacity under firm FTS contract by its in-service date, it is proposing to assign the costs associated with the 25,000 Dth per day of unsubscribed capacity (approximately $3 million) for recovery under its ITS and short-term FTS services.[23] Islander East also proposes an unauthorized overrun service under Rate Schedule FTS of $0.3605 per Dth which is based on 90 percent load factor rate for firm service.

2.

3. a. Recourse Rate

4.

5. Islander East's recourse rates are based on the following components: (1) $149,620,000 of gas plant in service, (2) a 14 percent return on equity (ROE), with an 8 percent cost of debt,[24] resulting in a 9.8 percent overall rate of return; (3) a capital structure of 70 percent debt and 30 percent equity; (4) 4 percent depreciation rate; (5) a federal tax rate of 35 percent and a 7.78 percent state tax rate; (6) billing determinates of 3,420,000 which is based on 100 percent thoughput for the 285,000 Dth capacity of the line; and (7) Operations and Maintenance expense of $5,785,149 which includes $4,785,150 for the Algonquin lease costs.

6.

7. The first year cost of service and the resulting rates are as follows:

8.

9.	Operation and Maintenance Expense	$ 5,785,149
10.	Depreciation Expenses	5,984,800
11.	Taxes Other than Income	3,299,715
12.	Federal Income Taxes	3,424,245
13.	State Income Taxes	825,375
14.	Return	14,428,973

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[23]As discussed below, as designed, Algonquin's proposed facilities can provide 260,000 Dth per day of firm capacity as required by the lease agreement and 25,000 Dth per day of interruptible capacity under certain circumstances.

[24]Islander East plans to seek the most favorable financing terms available in the marketplace at the time the project is financed and will use its actual cost of debt in calculating the rate it files prior to commencement of service.

15.	Total Cost of service	$33,748,257
16.		
17.	FTS Reservation Rate	
18.	Capacity (dth/d)	285,000
19.	Design Determinant	3,420,000
20.	Reservation Rate ($/Dth)	$9.868
21.		
22.	FTS Authorized Overrun Rate ($/Dth)	$0.3244
23.		
24.	FTS Usage-2 Rate (Reservation Rate	
25.	At 90% Load Factor) ($/Dth)	$0.3605
26.		
27.	ITS Usage Rate ($/Dth)	$0.3244

28.

29. We find Islander East's proposed recourse rate is reasonable, as conditioned below.

30.

31. b. Negotiated Rates

32.

33. Islander East requests negotiated rate authority for Rate Schedule FTS. We find that Islander East's proposal to offer negotiated rates conforms with the guidelines for negotiated rates as articulated in the Commission's Alternative Rate Policy Statement.[25] Under that policy, as affirmed in NorAm Gas Transmission Company (NorAm),[26] revenue shortfall due to the lower negotiated rates cannot be recovered from existing shippers. Therefore, our policy is to permit negotiated rates at lower than recourse rates in all cases, even to affiliates, and not only when lower rates are needed to compete for business. Accordingly, we will approve Islander East's proposed negotiated rate proposal, subject to Islander East maintaining separate and identifiable accounts for volumes transported, billing determinants, rate components, surcharges and revenues associated with its negotiated rates and to keep such information in sufficient detail so that it can be identified in future rate cases.

34.

35. Further, consistent with NorAm, Islander East will be required to file either its negotiated rate contract or tariff sheets that reflect the essential elements of its negotiated

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[25]Alternatives to Traditional Cost-of-Service Ratemaking for Natural Gas Pipelines and Regulation of Negotiated Transportation Services of Natural Gas Pipelines, 74 FERC ¶ 61,076 (1996), reh'g and clarification denied, 75 FERC ¶ 61,024 (1996), reh'g denied, 75 FERC ¶ 61,066 (1996); petition for review denied, Burlington Resources Oil & Gas Co. v. FERC, Case No. 96-1160, et al., U.S. App. Lexis 20697 (D.C. Cir. July 20, 1998).

[26]NorAm Gas Transmission Co. (NorAm), 77 FERC ¶ 61,011 (1996), order on reh'g, 81 FERC ¶ 61,204 (1997).

rate agreement in sufficient detail to enable shippers that believe they are similarly situated with respect to a particular negotiated rate customer to make such a determination.[27] In addition, Islander East's negotiated rate authority is subject to the Commission's policy regarding protecting the recourse rate-paying shippers against inappropriate cost-shifting with negotiated rates and discount adjustments,[28] and what deviations are permitted as part of a negotiated rate agreement.[29]

36.

37. c. Triennial Rate Review

38.

39. Consistent with Commission policy,[30] Island East is required to make a filing at the end of its first three years of its actual operation to justify its existing recourse rates. In its rate filing, Island East projected units of service should be no lower than those upon which its approved initial rates are based.[31] The filing must include a cost and revenue study in the form specified in section 154.313 of the Commission's regulations, updating cost-of-service data, including the cost of plant-in-service and a compression gas flow analysis, describing compression and operating pressure of all facilities. After review, we will be able to determine whether we should exercise our authority under NGA section 5 to establish just and reasonable rates.[32] Alternatively, in lieu of this filing, Islander East may make an NGA section 4 filing to propose alternative recourse rates to be effective no later than three years after the in-service date.

1. d. IT Revenue Crediting

2.

3. Although Islander East reports that it is proposing to assign the costs associated with the 25,000 Dth per day of unsubscribed capacity (approximately $3 million) for recovery under its ITS and short-term FTS services, its pro forma tariff fails to reflect the allocation of any costs to interruptible service. Consistent with the Commission's approach in similar cases, Islander East must allocate an appropriate level of the estimated cost of service to its interruptible service, recalculate its rates, and file

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[27] NorAm, 81 FERC at 61,872.

[28] Id.

[29] See ANR Pipeline Co., 97 FERC ¶ 61,222 (2001); 97 FERC ¶ 61,223 (2001); 97 FERC ¶ 61,224 (2001); Tennessee Gas Pipeline Co., 97 FERC ¶ 61,225 (2001).

[30] See, e.g., Petal Gas Storage, L.L.C., 97 FERC ¶ 61,097 (2001).

[31] Id.

[32] Id.

documentation demonstrating its recalculation. [33] Alternatively, Islander East may choose to credit the ITS revenues to its firm shippers, in which case Islander East must revise its tariff to provide for a mechanism to credit 100 percent of the ITS revenues, net of variable costs, to its firm recourse rate shippers.

4.

5. e. GISB and Order No. 637 Compliance

6.

7. The Commission has adopted in its regulations various standards for conducting business and electronic communication with interstate gas pipelines as promulgated by the Gas Industry Standard Board (GISB). The standards are intended to govern nominations, allocations, balancing measurement, invoicing, capacity release, and mechanisms for electronic communications between pipelines and those with whom they do business. In its pro forma tariff sheets, Islander East included standards that purport to comply with GISB requirements.

1. We will require Islander East to file pro forma tariff sheets 60 days from the order issuing a certificate that reflects the GISB standards as revised by the Commission at that time. The GISB standards in Islander East's pro forma tariff must either be incorporated by reference or incorporated verbatim. Further, Islander East must file a chart that identifies the location of the GISB standards in the tariff and those incorporated into the tariff verbatim. In addition, the revised pro forma tariff sheets must also reflect compliance with Order Nos. 637, 637-A, 637-B,[34] and subsequent orders concerning such issues as scheduling equality and discounting.[35] Islander East must file a detailed description of how its tariff fully complies with Order Nos. 637, et seq., along with a chart that identifies the location of the tariff changes made to comply with Order No. 637 and any other changes to its revised pro forma tariff.

2.

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[33] See, e.g., Horizon Pipeline Co., L.L.C., 92 FERC ¶ 61,205 (2000); Independence Pipeline Co., 89 FERC ¶ 61,283 (1999); and Maritimes and Northeast Pipeline, L.L.C., 80 FERC ¶ 61,136 (1997).

[34] Regulation of Short-Term Natural Gas Transportation Services, and Regulations of Interstate Natural Gas Transportation Service, Order No. 637, 65 FR 10,156 (Feb. 25, 2000), FERC Stats. & Regs., Regulation Preambles ¶ 31,901 at 31,308 (2000), order on reh'g, Order No. 637-A, 65 FR 35,706 (June 5, 2000), FERC Stats. & Regs., Regulation Preambles ¶ 31,099 (2000), 91 FERC ¶ 61,169 (2000); order denying reh'g, Order No. 637-B, 92 FERC ¶ 61,062 (2000).

[35] See Colorado Interstate Gas Co., 95 FERC ¶ 61,321 at 62,119-62,121 (2001); order on reh'g, 96 FERC ¶ 61,186 (2001) and Granite State Gas Transmission, Inc. 95 FERC ¶ 61,450 (2001), order on compliance, 96 FERC ¶ 61,273 at 62,036-62,037 (2001).

3. f. Cost Overruns

4.

5. The Policy Statement asserts that the risks of construction cost overruns should be apportioned between the pipeline and the new customers in their service contracts. Thus, in pipeline contracts for service on newly constructed facilities, pipelines should not rely on standard "Memphis clauses," but should reach agreement with new shippers concerning who will bear the risks of underutilization of capacity and cost overruns associated with the new construction.[36] Islander East's precedent agreements do not contain any risk-sharing language on construction costs. If the parties agree to risk sharing agreements, Islander East must file those agreements with the Commission as non-conforming service agreements with negotiated terms and conditions. The Commission will review those agreements to ensure that they are not unduly discriminatory or preferential.

1. When Islander East files its initial rates, we will allow it to modify the cost of service and resulting rates authorized herein to the extent necessary to reflect the actual cost of debt incurred to construct the project. However, if Islander East desires to make any other changes not specifically authorized by this order prior to placing its facilities into service, it will need to file an amendment to its application under section 7(c). In that filing, Islander East will need to provide cost data and the required exhibits supporting any revised rates. After the in-service date, Islander East must make an NGA section 4 filing to change its rate to reflect revised construction and operating costs.

2. 2. Algonquin's Rate Proposal

3.

4. Algonquin proposes to lease 285,000 Dth per day of capacity to Islander East from the interconnection of its mainline and C-System, in Cheshire, Connecticut to an interconnection with Islander East on the C-system in North Haven, Connecticut. Algonquin will provide the proposed capacity pursuant to the Capacity Lease and Operating Agreement (Lease Agreement) between Algonquin and Islander East. The primary term of the Lease Agreement is 20 years. Under the Lease Agreement, Algonquin will charge a fixed monthly lease payment of $334,135 for an annual payment of $4,009,620, which it contends will recover the costs associated with the construction of the leased facilities.

5.

6. Algonquin asserts that the proposed lease payment does not exceed its firm transportation rates for comparable service over the term of the lease and therefore is less than Islander East would incur if it had contracted for firm transportation service on

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[36] Policy Statement, 88 FERC at 61,747 (1999). "Memphis clause" refers to an agreement that the pipeline may change the rate during the term of the contract by making rate filings under NGA Section 4.

Algonquin. Algonquin argues that since the Lease Agreement does not provide flexible receipt and delivery points or capacity release rights and requires balancing on a daily basis, the reduced rate reflects the more limited nature of service under the Lease Agreement.

7.

8. Algonquin proposes the following revenue and expenses associated with the lease for the first year of service:[37]

9.

10.	Revenues		
11.		Lease Payments	$4,009,620
12.		O & M Reimbursements	387,690
13.		Property Tax Reimbursement	387,840
14.		Total Revenue	$4,785,150
15.			
16.	Expenses:		
17.		Depreciation Expense (1.81%)	$ 584,992
18.		Property Taxes	387,840
19.		Operation and Maintenance Exp.	387,690
20.		Total Expense	$1,360,522

21.

22.Algonquin states that the operating income from providing service to Islander East is $3,424,628.

23.

24. Algonquin proposes an incremental fuel reimbursement percentage designed to recover the increase in fuel usage associated with the leased capacity on the C-System. Algonquin reports that the fuel reimbursement percentage is 0.63 percent, which Algonquin would retain from gas Islander East delivers to Algonquin at the Islander East Receipt Point, with adjustments as mutually agreed upon by the parties to reflect actual fuel consumption. Algonquin indicates that since it is not proposing to roll in the construction costs associated with the new facilities during the term of the Lease Agreement, no cost shift will be borne by its existing customers.

25.

26. a. Depreciation Expense

27.

28. Algonquin proposes to depreciate the lease facilities at 1.81 percent resulting in a 55 year depreciation rate. Consolidated Edison, New England LDCs, and Northeast Energy all contend that Algonquin's proposal to depreciate the proposed facilities at 1.81 percent would leave Algonquin's customers responsible for a large portion of the cost of such facilities if the lease were not renewed at the end of its 20-year term. If the lease is

[37]See Exhibit N, Schedule 1 in Algonquin's application.

approved, Consolidated Edison contends that Algonquin's proposed facilities should be depreciated at a rate of 5 percent per year, reflecting the 20-year life of the lease. New England LDCs asserts that it would be more appropriate to fully amortize the cost of the facilities over the 20-year term of the lease to assure that existing customers are protected from any adverse rate impact of the proposed facilities.

29.

30. Algonquin responds that the depreciation rate for its proposed facilities will not impact existing shippers because it has not sought rolled-in treatment. Algonquin states that if it ever does propose to include any remaining undepreciated plant associated with this project in its rate base, it will have to seek authority to do so at that time. Algonquin states that its proposed depreciation rate is appropriate because the market for gas on Long Island will not expire with the end of the Islander East lease and use of the proposed facilities can be expected to continue past the 20-year term of the lease.

31.

32. When considering depreciation rates in NGA section 7(c) applications for an incremental rate, the Commission reviews the contract term and in this instance the lease term to determine at which rate the facilities will be fully amortized. The contract term or in some instances the lease term dictates the depreciation rate, particularly for incremental facilities.[38] To insure that the existing shippers suffer no adverse impact from an incremental expansion, it is appropriate for the facilities to be fully depreciated when the contract or lease expires so that the pipeline has fully recovered the costs of the expansion facilities. Fully amortizing the cost of Islander East's leased facilities to the 20-year term of the lease will insure that the existing customers are protected from any adverse rate impact at the conclusion of the Lease Agreement. Therefore, Algonquin will be required to revise its depreciation expense for book and rate purposes, recording a 5 percent depreciation rate based on the 20-year term of the lease to insure that the facilities are fully depreciated at the conclusion of the lease.

33.

34. b. At Risk Condition and Subsidization

35.

36. Calpine questions whether Algonquin's shippers are subsidizing the lease arrangement. Calpine states that it is unclear whether the incremental O&M charge and the property taxes are being covered by the payments required in the lease agreement. Calpine requests that the Commission place Algonquin at risk for the underrecovery of any lease-related costs.

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[38] Algonquin Gas Transmission Co. 77 FERC ¶ 61,291 (1996); order granting and denying reh'g, 81 FERC ¶ 61,220 at 61,938 (1997); Vector Pipeline, L.P., 85 FERC ¶ 61,083 at 61,305-61,306 (1998); Algonquin Gas Transmission Co., 87 FERC ¶ 61,262 at 61,990 (1999); and Dauphin Island Gathering Partners, 87 FERC ¶ 61,078 at 61,342 (1999).

37.

38. Algonquin states that approval of the lease and the associated reimbursement of related O&M expense and property taxes will have no impact upon Calpine (or other Algonquin shippers) even if such reimbursements are inadequate since these costs are not in the cost of service underlying Algonquin's current rates. Algonquin states that even if it were to propose to recover such costs in a future rate proceeding, the issue could be addressed at that time.

39.

40. In designing the lease payment and expenses reported in the application and noted above, Algonquin failed to include several key cost of service components, including, federal and state income taxes, return on equity, and debt cost. To insure that there will be no adverse impact on Algonquin's existing customers from the Islander East lease, we will require Algonquin to include in its tariff a provision that will guarantee Algonquin's customers are protected and will be no worse off as a result of the Islander East lease. This tariff provision requires Algonquin to maintain separate records of all the costs and revenues for the Islander East lease and compare the revenue responsibilities of Algonquin's customers with and without the proposed Islander East lease to insure that existing customers are protected from the cost of the leased facilities.[39]

41.

42. Algonquin must file this tariff provision in the compliance filing implementing any certificate the Commission should issue in this proceeding. The impact of the lease arrangement can be reviewed in NGA section 4 and 5 rate cases during the term of the lease. Further, if the lease is terminated prior to the expiration of the 20-year term, Algonquin will be required to explain and justify any changed rate treatment for the Islander East facilities and why the existing customers should be liable for the cost of an incremental facility. Such a provision insures that there will not be any subsidization by Algonquin's existing customers.

43.

44. The purpose of an "at-risk" condition was to protect a pipeline's existing customers from bearing the risks of unsuccessful projects. As explained above, the threshold requirement for new pipeline projects under the Policy Statement is that the pipeline be prepared to support the project financially without relying on a subsidy from existing customers. This usually means that projects will be priced incrementally, as is this project, so that the pipeline will be responsible for the costs of new capacity that is not fully utilized. Under those circumstances, the Commission no longer imposes at-risk conditions on pipeline projects.[40]

45.

46. c. Compressor Fuel Costs

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[39] See Cross Bay Pipeline, L.L.C., 97 FERC ¶ 61,165 at 61,758 (2001).

[40] See Northern Natural Gas Co., 94 FERC ¶ 61,191 (2001).

47.

48. To provide the proposed transportation service for Islander East, Algonquin intends to construct and operate a 10,310 horsepower compressor station. Calpine requests that the Commission clarify that Islander East would be responsible for all fuel use at this station, with no possibility that these fuel costs may be subsequently shifted to other Algonquin shippers.

49.

50. Algonquin states that the lease provides that the fuel retainage by Algonquin will be adjusted to reflect actual usage by Islander East, thereby insuring that Islander East will be accountable for the appropriate fuel. Algonquin adds that if it seeks to recover fuel attributable to the lease from other shippers, the issue can be addressed at that time.

51.

52. Since the transportation service is designed as an incremental rate, Islander East must be responsible for fuel reimbursement for operating the compressor station to provide the proposed service. To insure that Algonquin's existing customers are not subsidizing the fuel used to operate the compressor station, Algonquin must report the fuel costs separately in its fuel tracker, assessing Islander East a fuel charge to recover such costs, and cannot charge its other customers for fuel use to operate the compressor station that serves Islander East.

53.

54. d. Pre-tax Return

55.

56. Northeast Energy does not believe the lease payments provide an adequate pre-tax return on Algonquin's investment. Northeast Energy states that the lease would provide a 10.6 percent pre-tax return which is below the pre-tax return imbedded in Algonquin's current settlement rates. This, according to Northeast Energy, may be subsidization by Algonquin's existing customers. As stated, Algonquin cannot pass on any costs it fails to recover to its existing customers including any costs that may arise from a 10.6 percent pre-tax return.

57.

58. D. Design Capacity and Operating Conditions

59.

60. The Connecticut Companies assert that Algonquin has shown inconsistent delivery pressures for delivery at the North Haven gate station in its flow diagrams in this project (423 pounds per square inch (psig)) and in the HubLine Project (387 psig),[41] which threatens service to one of the Connecticut Companies. The Connecticut Companies ask that the Commission, at a minimum, require Algonquin to deliver gas at "an acceptable and predictable pressure level." Further, the Connecticut Companies claim the Islander East project will degrade service by threatening the existing level of hourly delivery

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[41] See, Maritimes & Northeast Pipeline, L.L.C., 95 FERC ¶ 61,077 (2001).

flexibility. The Connecticut Companies ask that the Commission require Algonquin to guarantee "the traditional level of hourly flexibility" that has previously been provided. Northeast Energy adds that Algonquin's flow diagrams do not indicate where Islander East's customers will source their gas supplies and how the movement of these supplies on Algonquin's system will affect existing customers.

61.

62. Algonquin asserts that the Connecticut Companies' claims of inconsistent pressures at the North Haven gate station is irrelevant. Algonquin states that the critical standard is whether the facilities can meet contractual pressure obligations. According to Algonquin, the contractual obligation is for a delivery pressure of 199 psig, well below the pressures in the flow diagrams. As to hourly flexibility, Algonquin states that it has designed its facilities to continue to meet its contractual hourly flow obligations, including the "6 percent hour" rights that Southern Connecticut (one of the Connecticut Companies) has. Further, Algonquin states that the Connecticut Companies' speculation is baseless and that, if anything, the increase in MAOP and addition of compression proposed by Algonquin should increase flexibility rather than reduce it.

63.

64. In response to Northeast Energy, Algonquin states that it is not conferring any mainline rights to flow gas to Islander East shippers. Algonquin maintains that gas can be transported to that point on an interruptible basis, by using released capacity, or by existing customers using the Islander East delivery point as a secondary point. Since no mainline path for the gas can be assumed, Algonquin asserts that there is no point to depicting hypothetical flows on its mainline.

65.

66. Analysis of Algonquin's new delivery design pressures at the Guilford and North Haven delivery points for Southern Connecticut indicate that the pressure will decrease to 331 psig and 387 psig, respectively. However, Algonquin's contractual pressure obligations for the Guilford and North Haven delivery points are 100 psig and 199 psig, respectively. Therefore, the reductions in pressure are well in excess of Algonquin's contractual obligations and provide an acceptable level of pressure for the Connecticut Companies. We also verify that the addition of compression on the C-System and the increase in MAOP will enable Algonquin to maintain line pressures and manage line pack for its existing and new shippers such that it can continue to meet the existing level of hourly delivery flexibility on the C-System.

67.

68. Northeast Energy's concern over the source of the gas supplies and how the movement of such supplies on Algonquin's system is unfounded. Algonquin's mainline will not be adversely impacted by the Islander East volumes because: (1) Islander East shippers do not have mainline entitlements above Algonquin's existing mainline capacity; and (2) the new facility modifications will reduce the C-System's dependency on mainline pressures to maintain contractual obligations. Therefore, we find that the existing customers on Algonquin's system will not be adversely affected by the transport

of volumes for Islander East shippers on Algonquin's system, no matter the source of gas supplies.
69.
70. In NGA section 7(c) cases, the Commission will review and approve the design capacity of a project. Analysis of Algonquin's proposal concludes that the facilities are properly designed to increase the capacity of the C-System sufficent to meet the 260,000 Dth per day of firm capacity required under the lease agreement. The design capacity of the C-System is based upon sound engineering practices that will ensure that the pipeline will be able to meet the design capacity on a year-round basis.
71.
72. We note, however, that the actual operating capacity may be greater on a day-to-day basis. The capacity of the C-System will depend upon several factors including (but not limited to): (1) the ambient temperature; (2) the actual available horsepower of compression at the Cheshire Compressor Station; (3) the mainline pressure at the interconnect of the C-System; and (4) lower delivery pressure at the terminus of Islander East's pipeline system. Any actual operating conditions that are different from the design assumptions included in the instant application could allow Algonquin to transport additional volumes of natural gas above the design capacity of 260,000 Dth per day (i.e., up to the total firm and interruptible lease capacity of 285,000 Dth per day). Even when Algonquin's system is operating under conditions more favorable than its design day by allowing Algonquin to transport greater volumes of natural gas on its C-System, Algonquin's mainline system will not be adversely impacted. Further, our analysis also concludes that the Islander East facilities are properly designed to transport the design capacity of 260,000 Dth per day and up to 285,000 Dth per day when factors change on Algonquin's C-System (as detailed above).
73.
74. E. Competing Projects
75.
76. The New York PSC urges the Commission to evaluate competing proposals to the Islander East project if they are timely filed. The Connecticut Siting Council states that the Commission should consider the need for the Islander East facilities in conjunction with other competing pipeline facilities. Presently, there are no other similar proposals before the Commission to provide gas service to the areas proposed by Islander East. However, we note that, as required by NEPA, the Commission will evaluate alternatives to Islander East's project in the EIS.
77.

78. F. Environment
79.
80. On July 3, 2001, Commission staff issued a Notice of Intent to Prepare an Environmental Assessment for the Proposed Islander East Pipeline Project and Request for Comments on Environmental Issues. This notice initiated the scoping process and requested comments to identify issues that be addressed in the appropriate NEPA document – environmental assessment or EIS. The scoping period identified issues and potential impacts. On October 4, 2001, Commission staff issued a Notice of Site Visit and Summary of Scoping Issues; Notice of Intent to Prepare an Environmental Impact Statement. The October 4, 2001 notice summarized the issues to be examined in the EIS into the following general categories: Need for Project and Location; Landowner Issues; Tidal and Inland Ecological Impacts; Human and Sociological Impacts; Long Island Sound Ecological Impacts; and Various Concerns. The EIS will also evaluate possible alternatives to the proposed projects or portions of the projects, and make recommendations on how to lessen or avoid impacts on the various resource areas.

1. A draft EIS will be published and mailed to Federal, state, and local agencies, public interest groups, interested individuals, affected landowners, newspapers, libraries, and the Commission's official service list for this proceeding. A comment period will be allotted for review of the draft EIS. All comments on the draft EIS will be considered and a final EIS will be published that will include recommendations to the Commission.
2.
3. G. Part 284, Subpart G Blanket Transportation Certificate
4.
5. Islander East has applied in Docket No. CP01-385-000 for a Part 284, Subpart G blanket transportation certificate, which is generally applicable to all interstate pipelines. Part 284, Subpart G blanket certificates provide natural gas pipelines certain automatic NGA section 7 natural gas transportation authorizations for individual customers under the terms of its contract and tariff. Because Islander East will become an interstate pipeline with the issuance of a certificate to construct, lease, and operate the proposed pipeline facilities, and because a Part 284, Subpart G blanket certificate is required for Islander East to offer transportation services, the Commission will preliminarily issue Islander East the requested Part 284 certificate authority.
6.
7. H. Part 157, Subpart F Blanket Construction Certificate
8.
9. Islander East also has applied in Docket No. CP01-386-000 for a Part 157, Subpart F blanket construction certificate, which is generally applicable to all interstate pipelines. Part 157, Subpart F blanket certificates accord natural gas pipelines certain automatic NGA section 7 facility and service authorizations and allows them to make several types of simplified prior notice requests for certain minimal section 7 facility and service authorizations. Because Islander East will become an interstate pipeline with the

issuance of a certificate to construct, lease, and operate pipeline facilities, we will also preliminarily issue Islander East the requested Part 157, Subpart F, blanket certificate.
10.
11. I. Conclusion
12.
13. For the above-discussed reasons, we find, subject to completion of our environmental review and Islander East's and Algonquin's acceptance of the conditions set forth below, that the benefits of Islander East's and Algonquin's proposals will outweigh any potential adverse effects and therefore will be consistent with the Policy Statement and NGA section 7. Accordingly, we are making preliminary determinations that the public convenience and necessity require the granting of the requested authorizations to Islander East and Algonquin.
14.
15. At a hearing held on December 19, 2001, the Commission, on its own motion, received and made a part of the record all evidence, including the application and exhibits thereto, submitted in this proceeding, and upon consideration of the record,
16.
17. The Commission orders:
18.
19. (A) A preliminary determination is made that Islander East's and Algonquin's application under NGA section 7(c) to construct, operate and maintain natural gas facilities and to lease pipeline capacity, as described and conditioned herein, and as more fully described in the application, would, on the basis of all pertinent non-environmental issues, be required by the public convenience and necessity.
20.
21. (B) Any certificate and authority issued in a final order in this proceeding will be conditioned, as discussed in this order, on the following:
22.

(1) Islander East and Algonquin completing the authorized construction within two years of the final order; and

(2) Islander East's and Algonquin's complying with paragraphs (a), (c), (e), and (f) of section 157.20 of the Commission's regulations;

(C) The preliminary determination made in Ordering Paragraph (A) above contemplates issuance, after completion of pending review of all environmental matters raised by the application, of a final order of the Commission determining that the proposals are required by the public convenience and necessity, in accordance with NEPA and NGA section 7(c).

(D) Islander East shall maintain separate books, accounts, and records for transportation provided under negotiated rates and for transportation provided under cost-based rates.

(E) Islander East shall file sixty days after the order issuing a certificate rates and pro forma tariff sheets consistent with the above discussion, GISB, Order No. 637 standards, and negotiated rate authority in effect at that time.

(F) Islander East shall make a filing within three years after its in-service date, either justifying its existing recourse rates or proposing alternative rates, as discussed in the body of this order.

(G) Algonquin shall modify its pro forma tariff by adding a provision, as discussed in the body of this order, requiring Algonquin to maintain separate records for the Islander East lease comparing the revenue responsibilities with and without the proposed lease and also provide for the tracking of fuel costs associated with Islander East's leased facilities.

(H) Algonquin shall revise its depreciation expense for book and rate purposes, recording a five percent depreciation rate based on the 20-year term of the lease.

(I) Islander East shall execute contracts for the level of service and for the terms of service represented in the precedent agreements prior to commencing construction.

(J) A preliminary determination is made in Docket No. CP01-385-000 to issue a blanket transportation certificate to Islander East under Subpart G of Part 284 of the Commission's regulations.

(K) A preliminary determination is made in Docket No. CP01-386000 to issue a blanket construction certificate to Islander East under Subpart F of Part 157 of the Commission's regulations.

(L) Motions to intervene out-of-time are granted.

(M) All answers, comments, and protests are accepted into the record.

By the Commission.

(S E A L)

Linwood A. Watson, Jr.,

Acting Secretary.

APPENDIX

INTERVENERS

Docket Nos. CP01-384-000, CP01-385-000, and CP01-386-000

AES Endeavor
Avery, Edward; Cherpak, Marietta; and Lagatolla, Deborah
Branford, Connecticut, Town of
Brookhaven Energy Limited Partnership
Brookhaven, New York, Town of
Calpine Energy Services, L.P.
Central Pine Barrens Joint Planning and Policy Commission
Chiocchio, Christine
Chiocchio, Vincent J.
CoEnergy Trading Company
Connecticut Attorney General's Office
Connecticut Department of Public Utility Control
Connecticut Office of Consumer Counsel
Connecticut Siting Council, State of
Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc.
Cram, Bernard
Del Vecchio, Robert and Donna Doris
Delle Donne, Dean F. and Susan C.
Dominion Transmission, Inc.
Dynegy Marketing and Trade
Enron North America Corp.
Gincavage, Raymond J.
Guilford, Connecticut, Town of
Iroquois Gas Transmission System, L.P.
Juniper Point Association
Kennedy, Edward M., Jr.
KeySpan Delivery Companies (KeySpan Energy NY, KeySpan Energy LI, KeySpan Energy NE)
Lang, Edward P.
Lazine, William G.
Lewis, Henry M.
Long Island Pine Barrens Society
Long Island Power Authority and LIPA
Mars, Rebecca and Stanley
McGuire, Kevin J.

Millennium Pipeline Company, L.P.
New England Local Distribution Companies
New York State Department of Environmental Conservation
New York State Electric & Gas Corporation
North Haven, Connecticut, Town of
Northeast Energy Associates
Northeast Utilities Service Company, on behalf of Yankee Gas Services Company
PanCanadian Energy Services Inc.
Pine Orchard Association
Public Service Commission of the State of New York
Save the Sound, Inc.
Schaffer, David
Southern Connecticut Gas Company and Connecticut Natural Gas Company
Tennessee Gas Pipeline Company
Tiernan, Charles E., III
Tilcon Inc. and Branford Steam Railroad
Transcontinental Gas Pipe Line Corporation
TransEnergie U.S. Ltd. And Cross Sound Cable Company, LLC
United States Postal Service

Docket No. CP01-387-000

ANP Bellingham Energy Company, LLC and Milford Power Limited Partnership
Avery, Edward; Cherpak, Marietta; and Lagatolla, Deborah
Calpine Energy Services, L.P.
Connecticut Attorney General's Office
Connecticut Department of Public Utility Control
Connecticut Office of Consumer Counsel
Connecticut Siting Council, State of
Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc.
Del Vecchio, Robert and Donna Doris
Dominion Transmission, Inc.
Dynegy Marketing and Trade
Enron North America Corp.
Gincavage, Raymond J.
Guilford, Connecticut, Town of
Iroquois Gas Transmission System, L.P.
KeySpan Delivery Companies (KeySpan Energy NY, KeySpan Energy LI, KeySpan Energy NE)
Lazine, William G.
Long Island Pine Barrens Society
Long Island Power Authority and LIPA
Millennium Pipeline Company, L.P.
New England Local Distribution Companies
New York State Electric & Gas Corporation
North Haven, Connecticut, Town of
Northeast Energy Associates
Northeast Utilities Service Company, on behalf of Yankee Gas Services Company
PanCanadian Energy Services Inc.
Southern Connecticut and Connecticut Natural Gas Corporation
Tennessee Gas Pipeline Company